United States Government Accountability Office

Testimony

Before the Committee on Oversight and Government Reform, House of Representatives

For Release on Delivery
Expected at 10 a.m. ET
Tuesday, February 7, 2017

U.S. POSTAL SERVICE

Key Considerations for Restoring Fiscal Sustainability

Statement of Lori Rectanus, Director, Physical Infrastructure Issues

Accessible Version

GAO-17-404T

GAO Highlights

Highlights of GAO-17-404T, a testimony before the Committee on Oversight and Government Reform, House of Representatives

Why GAO Did This Study

USPS is a critical part of the nation's communication and commerce, delivering 154 billion pieces of mail in fiscal year 2016 to 156 million delivery points. However, USPS's mission of providing prompt, reliable and efficient universal services to the public is at risk due to its poor financial condition. USPS's net loss was $5.6 billion in fiscal year 2016, its tenth consecutive year of net losses. At the end of fiscal year 2016, USPS had $121 billion in unfunded liabilities, mostly for retiree health and pensions, and debt—an amount equal to 169 percent of USPS's revenues.

In July 2009, GAO added USPS's financial condition to its list of high-risk areas needing attention by Congress and the executive branch. USPS's financial condition remains on GAO's High-Risk List. In previous reports, GAO has identified strategies and options for USPS to generate revenue, reduce costs, increase the efficiency of its delivery operations, and restructure the funding of USPS pension and retiree health benefits. GAO has also previously reported that a comprehensive package of actions is needed to improve USPS's financial viability.

This testimony discusses (1) factors affecting USPS's deteriorating financial condition, (2) USPS's ability to make required retiree health and pension payments, and (3) considerations and choices Congress faces in addressing USPS's financial challenges. This testimony is based primarily on past GAO work that has examined USPS's financial condition—including its liabilities—and updated USPS financial information for fiscal years 2016 and 2017.

View GAO-17-404T. For more information, contact Lori Rectanus at (202) 512-2834 or rectanusl@gao.gov.

February 7, 2017

U.S. POSTAL SERVICE

Key Considerations for Restoring Fiscal Sustainability

What GAO Found

The U.S. Postal Service's (USPS) deteriorating financial condition is unsustainable as a result of trends including:

- *Declining mail volume*: First-Class Mail—USPS's most profitable product—continues to decline in volume as communications and payments migrate to electronic alternatives. USPS expects this decline to continue for the foreseeable future.
- *Growing expenses:* Key USPS expenses such as salary increases and work hours continue to grow, due in part to growth in shipping and packages, which are more labor-intensive. Compensation and benefits comprise close to 80 percent of USPS's expenses.

USPS's financial condition makes it unlikely it will be able to fully make its required retiree health and pension payments in the near future. In fiscal year 2016, when USPS was required to make $13.0 billion in retiree health and pension payments, it made $7.0 billion in payments—mainly due to not making a required retiree health payment of $5.8 billion. USPS's required payments have been restructured for fiscal year 2017 and are estimated to total $10.3 billion. USPS's ability to make these 2017 payments will be further challenged due to:

- *Expiration of a temporary "exigent" rate surcharge:* USPS has said the April 2016 surcharge expiration is reducing its revenues almost $2 billion annually.
- *No new major cost savings initiatives planned:* USPS made efforts in recent years to right-size its operations, but has no current plans to initiate major new initiatives to achieve cost savings in its operations.

Large unfunded liabilities for postal retiree health and pension benefits—which were $73.4 billion at the end of fiscal year 2016—may ultimately place taxpayers, USPS employees, retirees and their beneficiaries, and USPS itself at risk. As GAO has previously reported, funded benefits protect the future viability of an enterprise such as USPS by not saddling it with bills after employees have retired. Further, with USPS retirees participating in the same health and pension benefit programs as other federal retirees, if USPS ultimately does not adequately fund these benefits and if Congress wants these benefits to be maintained at current levels, funding from the U.S. Treasury—and hence the taxpayer—would be needed to maintain the benefit levels. Alternatively, unfunded benefits could lead to pressure for reductions in USPS benefits or pay.

Congress faces difficult choices and tradeoffs to address USPS's financial challenges. The status quo is not sustainable. Considerations for Congress include the (1) level of postal services provided to the public and the affordability of those services, (2) compensation and benefits for USPS employees and retirees in an environment of revenue pressures, and (3) tension between USPS's dual roles as an independent establishment of the executive branch required to provide universal delivery service and as a self-financing entity operating in a business-like manner.

Chairman Chaffetz, Ranking Member Cummings, and Members of the Committee:

I appreciate the opportunity to be here today to discuss the varied challenges facing the U.S. Postal Service (USPS) and choices Congress faces in addressing USPS's ongoing financial challenges. USPS is a critical part of the nation's communication and commerce, delivering 154 billion pieces of mail in fiscal year 2016 to about 156 million delivery points, and with about 640,000 employees. USPS, however, continues to face a serious financial situation with insufficient revenues to cover its expenses, putting its mission of providing prompt, reliable, and efficient universal services to the public at risk.[1] USPS continues to incur deficits that are unsustainable. Moreover, at the end of fiscal year 2016, USPS had about $121 billion in unfunded liabilities and debt, most of which were for retiree health and pension benefits.[2] USPS continues to have $15 billion in outstanding debt—the statutory limit. These unfunded liabilities and debt are a large financial burden, increasing from 99 percent of USPS revenues in fiscal year 2007 to 169 percent of revenues in fiscal year 2016. USPS also recorded a net loss of $5.6 billion in fiscal year 2016—its tenth consecutive year of net losses totaling over $62 billion.

In July 2009, we added USPS's financial condition to our list of high-risk areas needing attention by Congress and the executive branch. USPS's financial condition continues to deteriorate and remains on our High-Risk List.[3] We have previously issued a number of reports that identified strategies and options for USPS to generate revenue, reduce costs, increase the efficiency of its delivery operations, and restructure the funding of USPS pension and retiree health benefits.[4] We continue to believe that a comprehensive package of actions is needed to improve USPS's financial viability.

[1] 39 U.S.C. § 101(a).

[2] Unfunded benefit liabilities are the estimated amount USPS has not sufficiently set aside to cover the benefits earned by its current and retired employees that are attributable to service already rendered.

[3] GAO, *High-Risk Services: An Update*, GAO-15-290 (Washington, D.C.: February 2015). An updated GAO high-risk report will be issued later this month.

[4] For example, our December 2012 report analyzed five different approaches for funding retiree health benefits and discussed the differing impacts that each alternative would have on USPS's future annual payments and unfunded liabilities. GAO, *U.S. Postal Service: Status, Financial Outlook, and Alternative Approaches to Fund Retiree Health Benefits*, GAO-13-112 (Washington, D.C.: Dec. 4, 2012).

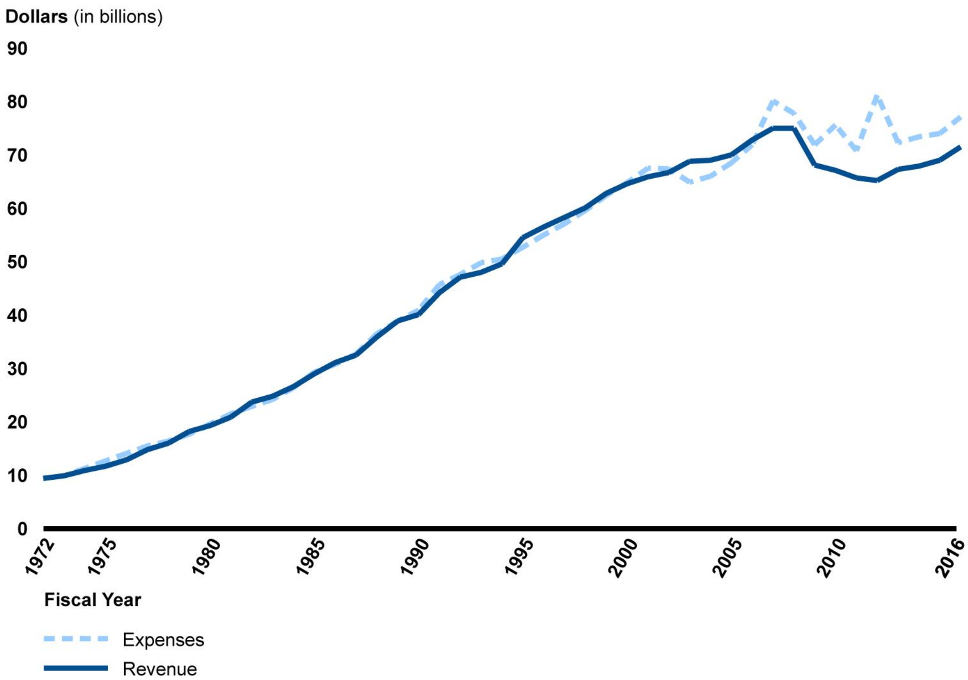
This testimony discusses: (1) factors affecting USPS's deteriorating financial condition, (2) USPS's ability to make required retiree health and pension payments, and (3) considerations and choices Congress faces in addressing USPS's financial challenges. This testimony is based primarily on our past reports and testimonies that examined USPS's financial condition, including its liabilities.[5] The reports and testimonies cited in this statement contain detailed information on the methods used to conduct our work. For this testimony, we updated USPS's financial information with reported results for fiscal year 2016, which ended September 30, 2016. In addition, we reviewed testimony and reports prepared by USPS and the Postal Regulatory Commission in 2016 and USPS estimates of retiree health and pension payments that USPS will be legally required to make in fiscal year 2017. We found these estimates to be sufficiently reliable for providing a general description and estimate for the large pending payments USPS faces. The work upon which this testimony is based was conducted in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

[5] GAO, U.*S. Postal Service: Continuing Financial Challenges and the Need for Postal Reform*, GAO-16-651T (Washington, D.C.: May 11, 2016); *U.S. Postal Service: Financial Challenges Continue,* GAO-16-268T (Washington, D.C.: Jan. 21, 2016); *U.S. Postal Service: Action Needed to Address Unfunded Benefit Liabilities,* GAO-14-398T (Washington, D.C.: Mar. 13, 2014); *U.S. Postal Service: Health and Pension Benefits Proposals Involve Trade-offs,* GAO-13-872T (Washington, D.C.: Sept. 26, 2013); *U.S. Postal Service: Proposed Health Plan Could Improve Financial Condition, but Impact on Medicare and Other Issues Should be Weighed before Approval*, GAO-13-658 (Washington, D.C.: July 18, 2013); *U.S. Postal Service: Status, Financial Outlook, and Alternative Approaches to Fund Retiree Health Benefits*, GAO-13-112 (Washington, D.C.: Dec. 4, 2012); *Federal Employees' Compensation Act: Analysis of Proposed Program Changes*, GAO-13-108 (Washington, D.C.: Oct. 26, 2012); *U.S. Postal Service: Allocation of Responsibility for Pension Benefits between the Postal Service and the Federal Government*, GAO-12-146 (Washington, D.C.: Oct. 13, 2011); and *U.S. Postal Service: Strategies and Options to Facilitate Progress toward Financial Viability*, GAO-10-455 (Washington, D.C.: Apr. 12, 2010).

Declining Mail Volume and Growing Expenses Contribute to USPS's Deteriorating Financial Condition

After about 30 years of relatively steady growth, USPS's expenses began consistently exceeding revenues in fiscal year 2007—a trend that has continued through fiscal year 2016 (see fig. 1). As a result, USPS has lost a total of $62.4 billion since fiscal year 2007.

Figure 1: U.S. Postal Service Revenue and Expenses, Fiscal Years 1972—2016



Source: U.S. Postal Service. | GAO-17-404T

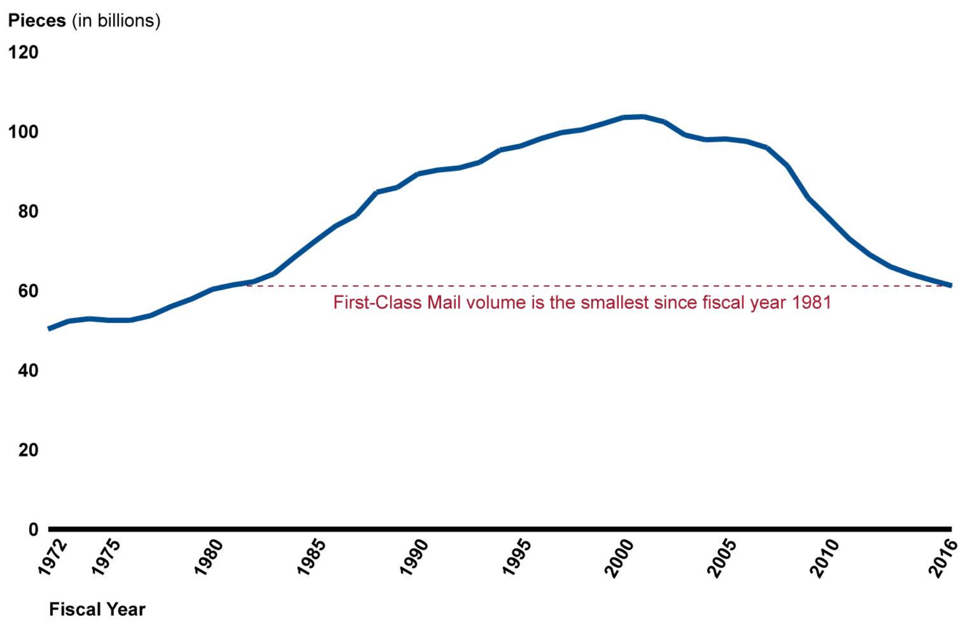
As we testified last year,[6] the continued deterioration in USPS's financial condition is due primarily to two factors.

1. *Declining First-Class Mail volumes:* The long-term decline of First-Class Mail volume, which USPS expects to continue for the foreseeable future, has fundamental implications for USPS's business

[6] GAO-16-651T and GAO-16-268T.

model because this remains USPS's most profitable class of mail. Domestic First-Class Mail volume declined by 2 percent in fiscal year 2016 from the previous fiscal year to 61 billion pieces—a level 41 percent below its peak in fiscal year 2001, and the smallest level since fiscal year 1981 (see fig. 2). USPS recently reported that First-Class Mail volume is declining as major commercial mailers actively promote the use of online services, and although the rate of decline has slowed, will continue to decline in future years with the migration to electronic alternatives resulting from technological changes.[7] In the long run, USPS also faces the possibility of a future economic downturn that could have an additional impact on First-Class Mail volume.

Figure 2: U.S. Postal Service First-Class Mail Volume, Fiscal Years 1972—2016



Source: U.S. Postal Service. | GAO-17-404T

Note: This chart shows domestic First-Class Mail volume.

2. *Growing Expenses:* USPS expenses increased by $3.1 billion in fiscal year 2016 from the previous year, outpacing the $2.6 billion increase in revenues. Increasing compensation and benefits expenses were a key driver of expense growth. USPS reported that compensation and benefits for active employees increased by $1.2 billion, due to

[7] United States Postal Service, *2016 Report on Form 10-K* (Washington, D.C: Nov. 15, 2016).

contractually obligated salary escalations and additional work hours associated in large part with growth in the more labor-intensive Shipping and Packages business.[8] In this regard, USPS reported a 14 percent growth in Shipping and Packages volume in fiscal year 2016.[9] However, to accommodate the surge in this volume and to minimize service disruptions during the holiday season, USPS reported increasing Sunday delivery service and adding non-career employees for the holiday season. This contributed to growth in USPS work hours in fiscal year 2016 from the previous year, when the number of USPS career employees increased by 17,000 and the number of non-career employees increased by 1,000. Over the past 3 years, the size of USPS's total workforce has increased by about 22,000, including career and non-career employees; this growth contrasts with the trend from fiscal years 1999 through 2013, when the workforce decreased by more than 288,000 (see fig. 3). Compensation and benefits comprise close to 80 percent of total USPS expenses. Thus, expenses will continue to grow if increases in salaries and work hours continue.[10,11]

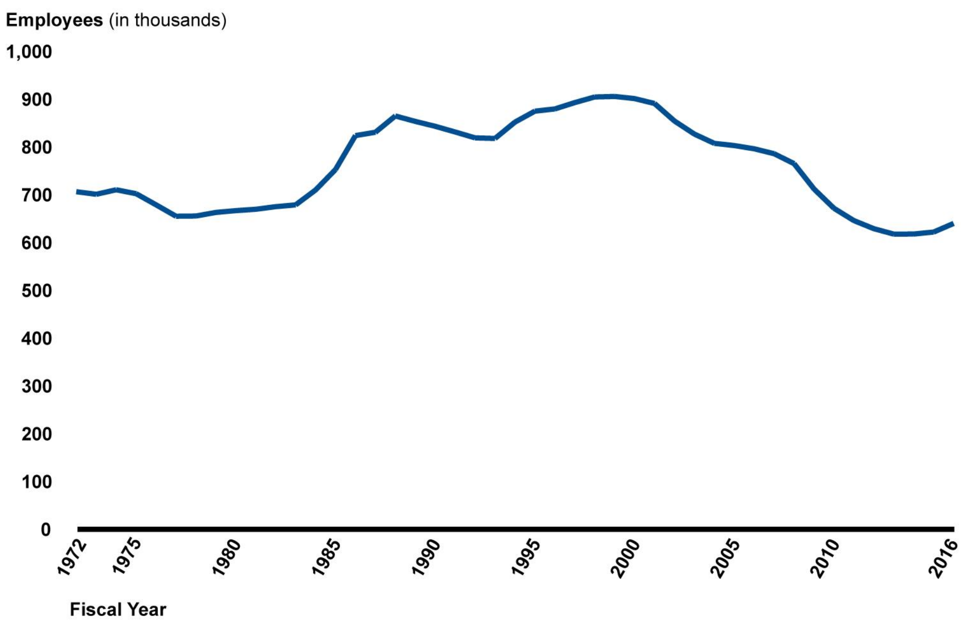
8 The Shipping and Packages category includes Priority Mail, Priority Mail Express, Parcel Select, First-Class Package Service, Standard Mail Parcel Service Parcel Return Service, and Package Services such as Bound Printed Matter, Media Mail, and Library Mail.

9 Growth in the volume of Shipping and Package Services and Standard Mail in fiscal year 2016 offset the decline in First-Class Mail volume. As a result, total mail volume increased by 0.1 percent in fiscal year 2016 to 153.9 billion pieces, which was 28 percent below its peak in fiscal year 2006.

10 USPS has budgeted for a $0.4 billion increase in compensation and benefits for fiscal year 2017 based on a number of factors, including an anticipated number of work hours similar to fiscal year 2016.

11 USPS's Total Factor Productivity (TFP) slightly declined in fiscal year 2016—the first time productivity declined since fiscal year 2009. TFP is an index that measures how efficiently USPS uses resources (inputs) to handle all aspects of its workload. See USPS, *FY2016 Annual Report to Congress* (Washington, D.C.: December 2016).

Figure 3: Total Number of U.S. Postal Service Employees, Fiscal Years 1972-2016



Source: U.S. Postal Service. | GAO-17-404T

Note: This graphic includes both career and non-career employees.

As previously discussed, USPS's unfunded liabilities and debt have become a large financial burden,[12] increasing from 99 percent of USPS revenues at the end of fiscal year 2007 to 169 percent of revenues at the end of fiscal year 2016. These unfunded liabilities and debt—totaling about $121 billion at the end of fiscal year 2016—consist mostly of retiree health and pension benefit obligations for which USPS has not set aside sufficient funds to cover.

[12] USPS's unfunded liabilities and debt as a percentage of its revenues declined to 169 percent at the end of fiscal year 2016 from 176 percent (an updated estimate) at the end of fiscal year 2015, largely due to growth in USPS revenues, which increased $2.6 billion in fiscal year 2016 from the previous year to $71.5 billion. In addition, USPS's unfunded liabilities and debt of $120.7 billion at the end of fiscal year 2016 was $0.9 billion less than the comparable figure at the end of the previous year. These totals included the latest Office of Personnel Management (OPM) estimates of unfunded USPS liabilities for postal pension benefits (projections for fiscal year 2016 and a revised estimate for fiscal year 2015), OPM valuations of unfunded liabilities for postal retiree health benefits, USPS estimates of liabilities for postal workers' compensation benefits, USPS debt, and other liabilities on USPS's balance sheet.

When the Postal Accountability and Enhancement Act (PAEA) established the Postal Service Retiree Health Benefits Fund, it required USPS to begin prefunding health benefits for its current and future postal retirees, with annual payments of $5.4 billion to $5.8 billion from fiscal years 2007 through 2016, followed by actuarially determined prefunding payments beginning in 2017 and every year thereafter.[13] As of the end of fiscal year 2016, USPS's liability for retiree health benefits was about $104.0 billion and the Postal Service Retiree Health Benefits Fund balance was $51.9 billion, with a resulting unfunded liability of $52.1 billion. USPS has missed a total of $33.9 billion in required prefunding payments, which represent about half of its total losses since fiscal year 2007.[14] However, USPS would have still lost $10.6 billion during this time period even without the annual prefunding requirement.

USPS Will Remain Unlikely to Fully Make Required Retiree Health and Pension Payments

USPS will remain unlikely to fully make its required retiree health and pension payments in the near future. Beginning this fiscal year (2017), USPS is no longer required to make fixed prefunding payments. Instead, under the requirements established by PAEA, it is required to start making annual payments based on actuarial determinations of the following component costs:

- a 40-year amortization schedule to address the unfunded liabilities for postal retiree health benefits,

[13] Pub. L. No. 109-435, § 803, 120 Stat. 3198 (2006), codified at 5 U.S.C. § 8909a. Under the prefunding mechanism established by PAEA, as implemented by the Office of Personnel Management (OPM), USPS payments into the Postal Service Retiree Health Benefits Fund (PSRHBF) would be projected to fund the liability over a period in excess of 50 years, from fiscal years 2007 through 2056 and beyond (with rolling 15-year amortization periods after 2041). PAEA established "fixed" prepayment amounts—meaning that the amounts were set by statute and did not vary with actuarial measurements of the cost of the benefits—in the first 10 years, from fiscal years 2007 through 2016, with actuarially determined payments thereafter. However, the payments required by PAEA were significantly "frontloaded," with the fixed payment amounts in the first 10 years exceeding what actuarially determined amounts would have been using a 50-year amortization schedule. For more detail, see GAO-13-112.

[14] For financial reporting purposes, missed prefunding payments are treated as USPS's expenses and reported as a liability on its balance sheet.

- the “normal costs” of retiree health benefits for current employees,[15] and
- a 27-year amortization schedule to address the unfunded liabilities for postal pension benefits under the Civil Service Retirement System (CSRS).[16]

These payments are in addition to annual payments USPS is already required to make to finance its pension benefits under the Federal Employees Retirement System (FERS)[17], which consists of a 30-year amortization schedule to address any unfunded liabilities, and the normal costs of FERS benefits for current employees. USPS will find it very difficult to make all of these required payments given its financial condition and outlook. As table 1 below shows, in fiscal year 2017, USPS will be required to make an estimated total of $10.3 billion in payments for retiree health and pension benefits under CSRS and FERS—about $3.3 billion more than what USPS paid in fiscal year 2016 for these benefit programs.

Table 1: U.S. Postal Service (USPS) Payments for Retiree Health and Pensions, Fiscal Years 2016 and 2017 (Dollars in Billions)

USPS payment	Fiscal year 2016 - Required	Fiscal year 2016 - paid	Fiscal year 2017 - required (estimate)
Retiree health benefits			
Health premiums	$3.3	$3.3	Not applicable
Fixed prefunding	$5.8	$0	Not applicable
Normal cost	Not applicable	Not applicable	$2.9
Amortization	Not applicable	Not applicable	$2.6
Pension benefits			
Civil Service Retirement System (CSRS)			
Amortization	Not applicable	Not applicable	$1.2

[15] The “normal cost” is the annual expected growth in liability attributable to an additional year of employees’ service.

[16] CSRS is a defined benefit, contributory retirement system for certain federal employees. It was replaced by the Federal Employees Retirement System (FERS) for federal employees who first entered covered service on and after January 1, 1987.

[17] In addition to providing an annuity at retirement based on years of service and “high-3” average pay, FERS also consists of Social Security and the government’s Thrift Savings Plan (TSP).

Federal Employees Retirement System (FERS)			
Normal cost	$3.7	$3.7	$3.3
Amortization	$0.2	$0[a]	$0.2
Total	$13.0	$7.0	$10.3[b]

Source: U.S. Postal Service. | GAO-17-404T

Note: Fiscal year 2017 estimates may change later this year when the Office of Personnel Management (OPM) provides USPS with the amounts of these required payments.

[a]USPS has not made its fiscal year 2016 FERS amortization payment and has a pending request that OPM reconsider this amount.

[b]Data do not add exactly to the total due to rounding.

In addition to declining mail volumes and increased expenses, USPS's ability to make its required payments for these retirement programs will be further challenged due to:

- *Expiration of a temporary rate surcharge:* USPS has reported that the April 2016 expiration of a 4.3 percent "exigent" surcharge that began in January 2014 is reducing its revenues by almost $2 billion annually.[18]
- *No new major cost-savings initiatives planned:* USPS has made efforts in recent years to right-size its operations to better adapt to declining mail volumes that are adversely affecting its financial position. For example, in fiscal year 2015, USPS reduced the hours of over 13,000 post offices to better match retail service with demand and reduced its physical footprint by consolidating 36 mail processing facilities, and instituted operational changes to better utilize resources. However, USPS has no current plans to initiate new major initiatives to achieve cost savings in its operations. According to USPS, it will continue to implement operational initiatives to contain costs and take

[18] In December 2013, the Postal Regulatory Commission (PRC) approved USPS's request for an "exigent surcharge" which allowed USPS to raise postal rates for most mail above the statutory price cap that is generally limited to the rate of inflation, except under extraordinary or exceptional circumstances that necessitate a larger rate increase. In July 2015, PRC ruled that USPS could continue the surcharge until it collected $4.6 billion in incremental revenue, which represents USPS's approximate loss due to the suppression of mail experienced during the Great Recession. This surcharge was discontinued April 10, 2016, resulting in the reduction of many postal rates, including the rate for a First-Class Mail stamp that was reduced from 49 to 47 cents. On January 22, 2017, the First-Class Mail stamp rate was increased to 49 cents as part of USPS pricing changes implemented under the statutory price cap. However, the January 2017 increase did not mitigate the continuing fiscal effects of the expiration of the exigent increase, which was an increase over the inflation-based cap.

actions to maintain liquidity,[19] but as we testified last year,[20] such actions will not be enough to stave off future losses and stabilize its finances. Although USPS has faced stakeholder resistance to its right-sizing efforts, in the absence of such efforts, USPS will continue to face challenges to appropriately match resources with mail volume and help address its compensation and benefits costs.

USPS has reported that without structural change to its business model and legislative change, it expects continuing losses and liquidity challenges for the foreseeable future.[21] According to USPS, it has maintained adequate liquidity only by not making required payments to prefund retiree health benefits and deferring needed capital investments. Looking forward, USPS has reported that, if circumstances leave it with insufficient cash, it may prioritize payments to its employees and suppliers ahead of some payments to the federal government, as it has done in the past.

Large unfunded liabilities for postal retiree health and pension benefits—which were $73.4 billion at the end of fiscal year 2016—may ultimately place taxpayers, USPS employees, retirees and their beneficiaries, and USPS itself at risk. As we have previously reported, funded benefits protect the future viability of an enterprise such as USPS by not saddling it with bills after employees have retired.[22] Further, since USPS retirees participate in the same health and pension benefit programs as other federal retirees, if USPS ultimately does not adequately fund these benefits and if Congress wants these benefits to be maintained at current levels, funding from the U.S. Treasury, and hence the taxpayer, would be needed to continue the benefit levels. According to USPS's testimony last year, "absent fundamental legislative reform, we face the prospect of

[19] To improve liquidity in recent years, USPS has reported conserving cash by spending only what it believed was essential to maintain its existing facilities and service levels. For example, although USPS said it must invest in upgrades of letter sorting equipment that is at or near the end of its useful life and also in equipment to fully capitalize on business opportunities in the growing package delivery market, it deferred facilities maintenance to conserve cash in instances where this could be done without adversely impacting employee health or safety issues.

[20] GAO-16-651T.

[21] For example, USPS has proposed statutory changes that would require postal retirees to participate in Medicare when they become eligible. This proposal would reduce USPS's expenses—and unfunded liability—for retiree health benefits because Medicare would become the primary insurer for all postal retirees.

[22] GAO-13-112.

having to continue to default on these prefunding payments [for retiree health benefits] in order to continue paying our employees and suppliers and to provide postal services to the American public. This increases the risk that taxpayers may ultimately be called on to fund these benefits."[23] Alternatively, unfunded benefits could lead to pressure for reductions in benefits or in pay. Thus, the timely funding of benefits protects USPS employees, retirees and their beneficiaries, taxpayers, and the USPS enterprise.

Congress Faces Difficult Choices to Address USPS's Financial Condition

USPS's financial situation leaves Congress with difficult choices and trade-offs to achieve the broad-based restructuring that will be necessary for USPS to become financially sustainable. USPS's ability to make its required retiree health and pension payments requires a decrease in expenses or increase in revenues, or both. Although USPS needs to take further action to reduce costs and increase revenues, USPS's actions alone under its existing authority will be insufficient to achieve sustainable financial viability; comprehensive legislation will be needed. Congressional decisions about how to address the following issues will shape USPS's future role, services, operations, networks, and ability to adapt to changes in mail volume. In making these decisions, Congress could consider, among other things, the following factors:

- *The level of postal services and the affordability of those services:* USPS's growing financial difficulties combined with vast changes in how people communicate provide Congress with an opportunity to consider what postal services will be needed in the 21st century. Specifically, Congress could consider what postal services should be provided on a universal basis to meet customer needs and how these services should be provided. Congress also could consider trade-offs in reducing the level of postal services, such as providing USPS with the authority to reduce the frequency of letter mail delivery to enable USPS to reduce its expenses. A key factor in any consideration to reduce postal services would include potential effects on postal customers, mail volumes, and employees. In particular, Congress

[23] USPS, *Statement of Megan J. Brennan, Postmaster General and Chief Executive Officer, United States Postal Service, Before the Senate Homeland Security and Governmental Affairs Committee* (Washington, D.C., Jan. 21, 2016).

could consider the quality of postal service—such as the frequency and speed of mail delivery and the accessibility and scope of retail postal services—in considering any service reduction. For example, as part of its efforts to reduce excess capacity, in January 2015 USPS revised its standards for on-time mail delivery by increasing the number of days for some mail to be delivered and still be considered on time. Even with the revised standards, on-time delivery performance declined significantly, particularly for the second quarter of fiscal year 2015, a decline USPS attributed to operational changes implemented in January 2015 and adverse winter weather. Performance has rebounded since then, facilitated in part by increases in workforce and mail transportation capacity and costs.

- *Compensation and benefits in an environment of revenue pressures:* Key compensation and benefits costs for USPS employees have increased and continue to increase, while the volume for First-Class Mail—USPS's most profitable product—has declined and continues to decline. To put USPS's situation into context, many private sector companies (such as automobile companies, airlines, mail preparation and printing companies, and major newspapers) took far-reaching measures to cut costs (such as reducing or stabilizing workforce, salaries, and benefits) when demand for their central product and services declined. However, although USPS has taken some steps to improve its financial situation, USPS has stated that its strategies to increase efficiency and reduce costs are constrained by statutory, contractual, regulatory, and political restrictions. USPS is subject to requirements to maintain 6-day delivery, limit rate increases for most mail within an inflation-based price cap, and participate in federal benefit programs. Most USPS employees are covered by collective bargaining agreements with four major labor unions which have established salary increases, cost-of-living adjustments, and the percentage of health insurance premiums paid by employees and USPS. When USPS and its unions are unable to agree, the parties are required to enter into binding arbitration by a third-party panel. There is no statutory requirement for USPS's financial condition to be considered in arbitration. Considering USPS's unsustainable financial condition and the competitive environment, we continue to believe—as we reported in 2010[24]—that Congress should consider revising the statutory framework for collective bargaining to ensure that USPS's financial condition be considered in binding arbitration.

[24] GAO-10-455.

- *USPS's dual role of providing affordable universal service while remaining self-financing:* As an independent establishment of the executive branch, USPS has long been expected to provide affordable, quality, and universal delivery service to all parts of the country while remaining self-financing. USPS and other stakeholders have considered a range of different business models to address USPS's financial difficulties. For example, USPS's 2002 Transformation Plan included a range of alternatives from a publicly supported model to a business model with a corporate structure supported by shareholders. Any alternative business model would need to address the level of any costs that would be transferred from USPS, which is financed by postal ratepayers, to the federal government, which is funded by taxpayers. In addition, if Congress requires eligible postal retirees to participate in Medicare, as USPS has previously proposed, it should consider the tradeoffs for the federal budget deficit and Medicare's financial condition, as well as the implications for affected employees.[25]

Finally, a fully functioning USPS Board of Governors is needed to support USPS's ability to carry out its critical responsibilities, as certain powers are reserved to the nine presidentially-appointed Governors who must be confirmed by the Senate. Because the last serving Governor left the Board in December 2016 due to term limits, the 11-member Board currently consists of only the Postmaster General and the Deputy Postmaster General. According to USPS, the critical responsibilities reserved to the Governors include setting postal prices, approving new products, and appointing or removing the Postmaster General and the Deputy Postmaster General. USPS stated last year that, in the event no Governors are in place, these critical duties may not be able to be executed, potentially leaving USPS without the ability to adjust its prices as needed, introduce new products, or appoint or replace its two most senior executive officers.

Conclusion

USPS management, unions, the public, community leaders, and Members of Congress need to take a hard look at what level of postal services residents and businesses need and can afford. The status quo is not sustainable.

[25] GAO-13-658.

Chairman Chaffetz, Ranking Member Cummings, and Members of the Committee, this concludes my prepared statement. I would be pleased to answer any questions that you may have at this time.

GAO Contact and Key Acknowledgments

For further information about this statement, please contact Lori Rectanus, Director, Physical Infrastructure Issues, at (202) 512-2834 or rectanusl@gao.gov. Contact points for our Congressional Relations and Public Affairs offices may be found on the last page of this statement. In addition to the contact named above, Frank Todisco, Chief Actuary, FSA, MAAA, EA, Applied Research and Methods; Derrick Collins, Assistant Director, Physical Infrastructure Issues; Samer Abbas; Antoine Clark; Kenneth John; Josh Ormond; Crystal Wesco; and Chad Williams made important contributions to this statement. Mr. Todisco meets the qualification standards of the American Academy of Actuaries to render the actuarial opinions contained in this testimony.

Appendix I: U.S. Postal Service (USPS) Financial Obligations and Related Information

Table 2: Selected U.S. Postal Service (USPS) Liabilities and Outstanding Debt (Dollars in Billions)

Fiscal year	Selected USPS liabilities (included on USPS balance sheet)			Funded status of Retiree Health and Pension Funds (not fully included on USPS balance sheet)			Totals			Unfunded obligations, liabilities, and debt as percentage of revenue
	Outstanding debt	Workers' compensation liabilities	Other liabilities	Funded status for retiree health benefits (unfunded)	Funded status for CSRS (unfunded)	Funded status for FERS (unfunded)	**Total USPS balance sheet assets**	**Total USPS liabilities, debt, and unfunded obligations**	**Total USPS revenue**	
2007	(4.2)	(7.8)	(12.7)	(55.0)	(3.1)	8.4	**25.8**	**(74.3)**	**75.0**	99%
2008	(7.2)	(8.0)	(12.5)	(53.5)	(9.0)	6.5	**26.0**	**(83.7)**	**75.0**	112%
2009	(10.2)	(10.1)	(13.2)	(52.0)	(7.3)	6.9	**28.1**	**(85.9)**	**68.1**	126%
2010	(12.0)	(12.6)	(13.6)	(48.6)	1.6	10.9	**24.3**	**(74.3)**	**67.1**	111%
2011	(13.0)	(15.1)	(14.2)	(46.2)	(17.8)	2.6	**23.4**	**(103.7)**	**65.7**	158%
2012	(15.0)	(17.6)	(13.7)	(47.8)	(18.8)	0.9	**22.6**	**(112.1)**	**65.2**	172%
2013	(15.0)	(17.2)	(12.5)	(48.3)	(17.8)	(0.1)	**21.6**	**(110.9)**	**67.3**	165%
2014	(15.0)	(18.4)	(12.5)	(48.9)	(19.4)	(3.6)	**23.0**	**(117.8)**	**67.9**	174%
2015	(15.0)	(18.8)	(12.5)	(54.8)	(16.7)	(3.8)	**24.0**	**(121.6)**	**69.0**	176%
2016	(15.0)	(20.0)	(12.3)	(52.1)	(17.5)	(3.8)	**25.2**	**(120.7)**	**71.5**	169%

Source: U.S. Postal Service (USPS) Form 10-K Statements. | GAO-17-404T

Note: This table provides data on selected USPS liabilities and outstanding debt at the end of each fiscal year as reported by USPS and the Office of Personnel Management (OPM). Key terms include the following:

Selected USPS liabilities include outstanding debt and workers' compensation liabilities, and other miscellaneous liabilities on USPS's balance sheet such as deferred revenue-prepaid postage, payables and accrued expenses, compensation and benefits liabilities (e.g., wages that have been earned but not yet paid as of the end of the fiscal year), and the value of employees' accumulated leave. Not included is the current liability for the statutory Postal Service Retiree Health Benefits Fund (PSRHBF) payments not yet paid by USPS, which is a component of the unfunded liability for retiree health benefits, and is also highlighted in table 4 in the "Total" line for the column labeled "Missed USPS prefunding payments."

Outstanding debt is total USPS short-term and long-term debt.

USPS liabilities for workers' compensation are the actuarial present value of future workers' compensation payments that USPS is estimated to have to make for injuries that have already occurred.

Unfunded actuarial liabilities for retiree health benefits are OPM estimates as of the end of each fiscal year. The unfunded liabilities are the excess of liabilities over funded assets. The liabilities represent the actuarial present value of the cost of the portion of future retiree health premiums for which USPS is responsible and that are attributable to past service; these liabilities reflect all such projected future costs for current retirees and beneficiaries and a portion of such projected future costs for current workers. The portion ($33.9 billion) of the fiscal year 2016 $52.1 billion unfunded liability that is attributable to the missed prefunding payments is reflected as such on USPS's balance sheet; the remainder ($18.2 billion) of the $52.1 billion unfunded liability is not on USPS's balance sheet.

Unfunded Civil Service Retirement System (CSRS) and Federal Employee Retirement System (FERS) actuarial liabilities are OPM estimates as of the end of each fiscal year. The unfunded liabilities are the excess of liabilities over funded assets. The liabilities represent the actuarial present value of the cost of future retiree pension benefits for which USPS is responsible and that are attributed to past service; these liabilities reflect all such projected future costs for current retirees and beneficiaries and a portion of such projected future costs (in excess of worker contributions) for current workers.

Unfunded obligations, liabilities, and debt are the sum of the unfunded actuarial liabilities (obligations), USPS liabilities, and debt shown in this table.

Total USPS revenue consists of total USPS operating revenue plus interest and investment income for each fiscal year.

Total assets consist of current assets including cash and noncurrent assets largely comprising property and equipment measured at historic purchase value after depreciation. This does not include assets funding the retiree health and pension benefits.

Table 3: Funded Status of U.S. Postal Service (USPS) Pension Obligations (Dollars in Billions)

Fiscal year	CSRS funded status			FERS funded status			Total USPS Pension funded status		
	CSRS assets	**CSRS actuarial liabilities**	**Net CSRS funded Status (unfunded)**	**FERS assets**	**FERS actuarial liabilities**	**Net FERS funded status (unfunded)**	**Pension assets**	**Pension actuarial liabilities**	**Total pension funded status (unfunded)**
2007	193.8	196.9	(3.1)	63.5	55.1	8.4	257.3	252.0	**5.3**
2008	195.1	204.1	(9.0)	69.3	62.8	6.5	264.4	266.9	**(2.5)**
2009	195.3	202.6	(7.3)	75.2	68.3	6.9	270.5	270.9	**(0.4)**
2010	194.6	193.0	1.6	80.8	69.9	10.9	275.4	262.9	**12.5**
2011	193.0	210.8	(17.8)	86.6	84.0	2.6	279.6	294.8	**(15.2)**
2012	190.7	209.5	(18.8)	91.7	90.8	0.9	282.4	300.3	**(17.9)**
2013	186.6	204.4	(17.8)	96.5	96.6	(0.1)	283.1	301.0	**(17.9)**
2014	182.1	201.5	(19.4)	100.9	104.5	(3.6)	283.0	306.0	**(23.0)**
2015	177.4	194.1	(16.7)	105.2	109.0	(3.8)	282.6	303.1	**(20.5)**
Projected 2016	174.4	191.9	(17.5)	112.1	115.9	(3.8)	286.5	307.8	**(21.3)**

Source: U.S. Postal Service (USPS) Form 10-K Statements. | GAO-17-404T

Note: This table provides the Office of Personnel Management's (OPM) estimation of the funded status of the Civil Service Retirement System (CSRS) and Federal Employee Retirement System (FERS) programs for USPS, as of the end of each fiscal year. Data are actual amounts for fiscal years 2007—2015 and projected amounts for fiscal year 2016. Key terms include the following:

Assets include securities of the Civil Service Retirement and Disability Fund (CSRDF). Although CSRDF is a single fund that does not maintain a separate account for each participating U.S. government employer, PAEA requires certain disclosures regarding obligations and changes in net assets as if the funds were separate.

Actuarial liabilities are actual amounts for fiscal years 2007—2015 and projected amounts for fiscal year 2016, as of the end of each fiscal year. These data are prepared by OPM and represent the actuarial present value of the cost of future retiree pension benefits for which USPS is responsible and that are attributed to past service; these liabilities reflect all such projected future costs for current retirees and beneficiaries and a portion of such projected future costs for current workers.

Net funded status equals assets minus liabilities.

Table 4: U.S. Postal Service (USPS) Retiree Health Benefits Funded Status (Dollars in Billions)

Fiscal year	Beginning of year assets	One-time transfer from CSRS pension fund	One-time transfer from USPS escrow	USPS prefunding payment	Interest earned	End of year assets	End of year actuarial liabilities	End of year net funded status (unfunded)	Missed USPS prefunding payments
2007	0.0	17.1	3.0	5.4	0.3	25.7			0.0
2008	25.7	N/A	N/A	5.6	1.3	32.6	86.1	(53.5)	0.0
2009	32.6	N/A	N/A	1.4	1.5	35.5	87.5	(52.0)	0.0
2010	35.5	N/A	N/A	5.5	1.5	42.5	91.1	(48.6)	0.0
2011	42.5	N/A	N/A	0.0	1.6	44.1	90.3	(46.2)	0.0
2012	44.1	N/A	N/A	0.0	1.6	45.7	93.6	(47.9)	11.1
2013	45.7	N/A	N/A	0.0	1.6	47.3	95.6	(48.3)	5.6
2014	47.3	N/A	N/A	0.0	1.5	48.9	97.7	(48.9)	5.7
2015	48.9	N/A	N/A	0.0	1.5	50.3	105.2	(54.8)	5.7
2016	50.3	N/A	N/A	0.0	1.5	51.9	104.0	(52.1)	5.8
2017	51.9	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Total	**N/A**	N/A		**17.9**	**13.9**	**N/A**	**N/A**	**N/A**	**33.9**

Source: U.S. Postal Service (USPS) Form 10-K Statements. | GAO-17-404T

Note: This table provides the Office of Personnel Management's (OPM) estimation of the funded status of USPS obligations for retiree health benefits. Data for assets, liabilities, and net funded status are actual amounts for fiscal years 2007—2016. Key terms include the following:

Assets include securities of the PSRHBF, which is managed by OPM.

Actuarial liabilities represent the actuarial present value of the cost of the portion of future retiree health premiums for which USPS is responsible and that are attributable to past service; these liabilities reflect all such projected future costs for current retirees and beneficiaries and a portion of such projected future costs for current workers.

Net funded status equals assets minus liabilities.

One-time transfer from the Civil Service Retirement System (CSRS) Pension Fund: The Postal Accountability and Enhancement Act (PAEA) established the PSRHBF and directed OPM to determine any USPS surplus for CSRS obligations as of Sept. 30, 2006, and to transfer this amount from the Civil Service Retirement and Disability Fund (CSRDF) into the PSRHBF by June 30, 2007. Pub. L. No. 109-435 (2006).

One-time transfer from USPS Escrow Fund: PAEA required USPS to transfer the escrow funds resulting from the Postal Civil Service Retirement System Funding Reform Act of 2003 (Pub. L. No. 108-18), which reduced USPS's CSRS payments and required these reductions to be placed into escrow.

USPS prefunding payments are statutory payments established by PAEA that are due from USPS to the PSRHBF. Subsequent congressional action reduced the 2009 prefunding requirement from $5.4 billion to $1.4 billion and delayed $5.5 billion from fiscal year 2011 to fiscal year 2012, resulting in a requirement to pay $11.1 billion in fiscal year 2012. See 5 U.S.C § 8909a(d)(3)(A).

Missed Prefunding Payments have not been made by USPS and remain as current liabilities on USPS's balance sheet. These amounts are reflected in this table through a lower asset total and higher net unfunded liability than would have occurred if the prefunding payments were made.

Table 5: Summary of U.S. Postal Service (USPS) Pension and Retiree Health Benefit (RHB) Funds (Dollars in Billions)

Fiscal year	Total USPS Pension funded status			USPS RHB fund status			Total Pension & RHB summary		
	Total pension assets	**Total pension actuarial liabilities**	**Total pension funded status (unfunded)**	**RHB assets**	**RHB actuarial liabilities**	**RHB funded status (unfunded)**	**Total assets**	**Total actuarial liabilities**	**Pension and retiree health benefit funded status (unfunded)**
2007	257.3	252.0	5.3	25.7	80.8	(55.0)	**283.0**	**332.8**	**(49.7)**
2008	264.4	266.9	(2.5)	32.6	86.1	(53.5)	**297.0**	**353.0**	**(56.0)**
2009	270.5	270.9	(0.4)	35.5	87.5	(52.0)	**306.0**	**358.4**	**(52.4)**
2010	275.4	262.9	12.5	42.5	91.1	(48.6)	**317.9**	**354.0**	**(36.1)**
2011	279.6	294.8	(15.2)	44.1	90.3	(46.2)	**323.7**	**385.1**	**(61.4)**
2012	282.4	300.3	(17.9)	45.7	93.6	(47.9)	**328.1**	**393.9**	**(65.8)**
2013	283.1	301.0	(17.9)	47.3	95.6	(48.3)	**330.4**	**396.6**	**(66.2)**
2014	283.0	306.0	(23.0)	48.9	97.7	(48.9)	**331.9**	**403.7**	**(71.9)**
2015	282.6	303.1	(20.5)	50.3	105.2	(54.8)	**332.9**	**408.3**	**(75.4)**
2016	286.5	307.8	(21.3)	51.9	104.0	(52.1)	**338.4**	**411.8**	**(73.4)**

Source: U.S. Postal Service (USPS) Form 10-K Statements. | GAO-17-404T

Note: This table provides the Office of Personnel Management's (OPM) estimation of the funded status of USPS obligations for pensions and retiree health benefits. Data for assets, liabilities, and net funded status are actual amounts for fiscal years 2007—2016 for retiree health benefits, and actual amounts for fiscal years 2007—2015 and projected amounts for fiscal year 2016 for pension benefits, as of the end of each fiscal year. Key terms include the following:

Assets include securities of the Civil Service Retirement and Disability Fund (CSRDF) and the Postal Service Retiree Health Benefits Fund (PSRHBF). Although CSRDF is a single fund that does not maintain a separate account for each participating U.S. government employer, PAEA requires certain disclosures regarding obligations and changes in net assets as if the funds were separate.

Actuarial liabilities are actual amounts for fiscal years 2007—2016 for retiree health benefits, and actual amounts for fiscal years 2007—2015 and projected amounts for fiscal year 2016 for pension benefits, as of the end of each fiscal year. These data are prepared by OPM and represent the actuarial present value of the cost of future retiree pension and health benefits costs for which USPS is responsible and that are attributed to past service; these liabilities reflect all such projected future costs for current retirees and beneficiaries and a portion of such projected future costs for current workers.

Net funded status equals assets minus liabilities.

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